

DEFENCE

CHAPTER FOUR

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PROGRAM OF ADMINISTRATIVE SAVINGS

Defence is required to achieve at least \$200m per annum in savings by 2003-04 as part of the Defence White Paper resourcing strategy. These savings targets have been met through a range of targeted measures in 2001-02 and 2002-03, as set out most recently in the *Portfolio Additional Estimates Statements 2002-03*, and by re-baselining the non-capability-related elements of internal Group budgets from 2003-04 onwards.

Defence recognises the need to continue to identify further savings and administrative efficiencies in 2003-04, and beyond, particularly to offset a range of unavoidable cost pressures, including:

- rising salary and wage and military allowance costs over and above the level of price augmentation to the Defence budget;
- rising Comcover insurance premiums; and
- ensuring adequate funding for maintenance of facilities and other infrastructure.

A program of administrative savings that is designed to free up funds to offset unavoidable cost pressures has been agreed by the Government and is built around four key themes:

- Group support arrangements, including remaining overlaps in common service delivery;
- further outsourcing activities, where these do not affect military workforce numbers;
- a range of financial transformation projects, including improved purchasing and payment arrangements; and
- reductions in overheads, where these are growing at unsustainable levels, including civilian personnel numbers, professional service providers and travel. In addition, there will be a reduction in the numbers of non-operational Defence personnel posted overseas.

The program of administrative savings will deliver ongoing cash savings of \$200m over and above the savings required as part of the Defence White Paper within a timeframe of five years, as shown in the table below.

Table 4.1: Administrative Savings Targets

	2003-04	2004-05	2005-06	2006-07	2007-08	Ongoing
	\$m	\$m	\$m	\$m	\$m	\$m
Savings target	50	100	150	175	200	200

DEFENCE MANAGEMENT REFORMS AND EFFICIENCIES

PROGRESS ON BUDGET REFORM

In 2000, Defence and the Department of Finance and Administration conducted a joint review of Defence's financial management arrangements, resulting in the presentation to, and acceptance, by the Government of a series of budget reform measures. Defence has subsequently undertaken a range of improvements to its business systems and processes. Substantial progress has been made in improving the financial and materiel management arrangements within Defence, although this work is not yet complete.

The key features of the Defence business model are:

- A focus on the achievement of Defence outcomes and the delivery of Defence outputs to the Government, with regular reporting to the Government on financial and non-financial performance.
- Accountability from the Minister's directive to the Secretary of the Department of Defence and the Chief of the Defence Force and, consequently, to Group Heads through charters and a cascading series of performance agreements, which align individual responsibilities with organisational goals and performance at all levels.
- A strategy-focused planning framework, driven by the Defence White Paper and *Australia's National Security: A Defence Update 2003*, which identifies key objectives and risks, and focuses on the means for achieving objectives.
- The annual development of a Defence Management and Finance Plan which sets our planned performance and funding over a 10-year period.
- The introduction of customer-supplier arrangements, which set out responsibilities for service delivery and align planned performance with funding allocations.
- An accrual financial framework which recognises the full cost of Defence activities, including the impact of significant assets and liabilities. In 2003-04, there will be increased emphasis on budgeting and monitoring cash at portfolio, outcome and output levels.
- The adoption of risk management principles, with the identification of significant risks at all levels and the allocation of responsibility for their management.
- A balanced scorecard which provides the mechanism for regular monitoring and reporting financial and non-financial performance across all Defence outputs, key processes, projects and activities.



Defence has implemented an output-based budgeting information system. Financial reporting on an output basis was implemented successfully for 2001-02 accounts, and the 2003-04 Defence Management and Finance Plan also was developed using this tool. Further development of this system will take place in 2003-04 to support new reporting and information management requirements. Each of the 15 Group executives has signed organisational performance agreements with the Secretary and the Chief of the Defence Force covering both the budget year and a 10-year forward view of resources and planned performance at the Group level.

In 2003-04, there will be a focus on improving the performance information and applying customer-supplier agreements between outcome executives and enabling executives. The agreements will have an emphasis on better defining the products and services to be delivered and their scope and cost. Work is continuing on the development of reliable pricing models for Defence's internal products and services that can be used to support a more results-focused resource allocation model.

Defence has improved its financial statement processes over the past year, reducing the number of significant issues of concern to the Australian National Audit Office (known as 'Category A' findings) from thirteen to eight. While the audit office's report on the 2001-02 financial statements was qualified, the qualification related to 'unquantified' uncertainties in relation to the price of inventory and the price and quantity of repairable items. The price and quantity uncertainties arose from system deficiencies in Defence's main supply-chain system.

Improving the quality of the financial statements involves a continuing process of data integrity checking and, over the next year, will also involve a system upgrade for better management of inventory items and purchases. Defence will continue to explore every practical means of eliminating the audit qualification, noting however the large volume of inventory items with uncertain prices and that the items concerned will be consumed over a number of years.

In terms of the wider reform agenda, implementation in Defence will take several years to reach fruition. Considerable progress has been made in acquisition and materiel reform, focusing on whole-of-life capability management based on partnerships with industry. Additionally, many recent projects are showing the benefits of the reform program, though substantial progress is still to be made. A Defence procurement review is currently under way to help shape priorities for the next stages of the reform.

Defence is also in the midst of wide-ranging reforms to its systems and management and business processes. A number of finance transformation projects are designed to improve Defence's business processes and financial management arrangements which will enhance transparency of information for decision making and accountability for results. Notable projects in 2003-04 include:

- the development of decision support tools that will provide information on the actual cost of defence force elements and products, and provide a single point of reference for key performance and resource information;

- further development of PMKeyS (Defence's main personnel management information system) through a more comprehensive reporting capability as well as the introduction of additional quality assurance functionality; and
- a more comprehensive approach to simple procurement, purchasing and the payment of accounts across Defence.

DEFENCE MATERIEL REFORM

The Defence Materiel Organisation ensures the oversight and management of support to military capabilities through acquisition and through-life support. The materiel reform program encompasses a comprehensive range of measures to:

- integrate the acquisition and support elements of the materiel organisation's business and locate these functions appropriately with customers;
- reform its processes, based on commercial approaches and best practice;
- adopt a more strategic approach to its relationship with industry;
- improve its relationship with stakeholders and customers; and
- create a climate in which people are valued and can do their best.

The Senate Foreign Affairs, Defence and Trade References Committee inquiry into materiel acquisition and management in Defence, tabled in March 2003, and the Defence procurement review, to be presented to the Minister for Defence later in this calendar year, will help shape future directions for materiel reform.

Priorities for 2003-04

Priorities for 2003-04 include:

- information systems - to rationalise information systems to manage business better;
- process documentation - to deliver and communicate better the organisation's new policies and processes in order to conduct Defence business on time, on budget and on schedule;
- communication - to improve communication with internal and external stakeholders to enhance performance;
- performance reporting - to rationalise reporting mechanisms to reduce duplication of effort and improve information;
- people issues - to continue to improve recruitment, development and retention to get the right people in the right positions at the right time;
- logistics cost drivers - to improve the understanding of logistics cost drivers, with an early emphasis on the development of a framework to assess shortfalls; and
- organisational services - to improve coordination of corporate activities and have a consistent approach to business, without duplication.

Initiatives for 2003-04

Organisational Reforms

These reforms include:

- continuing to refine the role of project governance boards for better governance of projects; and
- developing and implementing long-term strategies for selected key industry capabilities that support the ADF.

Process Reforms

These reforms include:

- applying best practice across the capability life cycle to increase the clarity of outcomes and outputs;
- improving the 'two pass' project approval process with a greater emphasis on the requirements for 'first pass' approval. The 'two pass' approach ensures that the Government is able to exert early direction over the major capital investment program;
- implementing guidelines for the capability development process which will lead to better requirement specifications and quality of information for the Government;
- introducing a new project management methodology for acquisition and management of major capital equipment that better reflects Defence business accountability and decision-making requirements;
- progressing a software acquisition program to improve cost estimation for software-intensive projects, as well as improving competence in software acquisition;
- improving the level of systems engineering capability in the organisation;
- implementing a quality and environmental management system;
- continuing to streamline procurement and contracting templates on recognised best practice to lower tendering and contracting costs for Defence and industry;
- developing improved methods for costing logistics requirements against Defence preparedness objectives;
- placing greater emphasis on a contractor's past performance in tender selection; and
- continuing to implement the use of 360-degree scorecards to assess the organisation's project performance from an industry perspective.

People Reforms

These reforms include:

- identifying career-stream competencies and skills to provide a basis for future recruitment and training; and
- continuing to develop workforce plans and strategies in project, financial and contract management, as well as aeronautical, systems and software engineering.

DELIVERING INTERNAL SERVICES

Corporate Services and Infrastructure Group comprises some 4,400 Australian Public Service and 1,700 ADF personnel who help create the working and living environment for Defence people. With representatives on most Defence sites around the country, the Group provides essential services and everyday support to more than 90,000 personnel. In this way, the Group is one of the vital elements underpinning Defence capability, as well as being central to the communities in which Defence operates.

Corporate Support and Infrastructure Group Corporate Plan 2003-04

In 2003-04, the Group's challenge will be to continue to improve the quality of Defence's infrastructure and the services provided to customers within a constrained budget. The Group will continue to support Defence's reform agenda by focusing on delivering strategic objectives that provide assurance to our owner, customers and stakeholders. The strategic objectives for 2003-04 are that:

- customers are confident about the Group's products, service, performance and cost;
- customers understand what the Group provides and can easily access its services;
- the Group is recognised as a high performing organisation that delivers best value for money and achieves planned performance; and
- the Group delivers sound stewardship of its resources in order to contribute to the sustainable delivery of Defence outcomes.

In delivering these strategic objectives, the key priorities are to:

- implement sound and economical savings strategies to direct resources in support of capability and operations; and
- maintain project 'Next Steps' which aims to provide better service, enhance the Group's strategic planning capability and articulate the relationship and accountabilities shared between national and regional offices.

Planned Initiatives for 2003-04

National Operations

Planned initiatives to be progressed in 2003-04 include:

- conducting relationship reviews with the three Services and key stakeholders and continuing a rolling program of relationship reviews;
- completing base-level customer service agreements;
- restructuring the National Operations Division to improve customer support, including the establishment of a joint operations support staff and better alignment of technical authority streams with the division;
- updating environmental management plans and developing environmental management systems;
- pursuing cost savings and efficiency improvements;
- bedding down regional and base structures, including customer service centres;
- delivering major customer improvements, such as training range upgrades;
- completing the development of processes and procedures for management of facilities operations within a devolved regional environment;
- redeveloping garrison support and comprehensive maintenance contracts; and
- ensuring effective governance and stewardship of assets.

Information Systems

Planned initiatives to be progressed in 2003-04 include:

- developing a transparent business planning framework;
- retiring legacy applications;
- developing a wide-area-network resiliency and contingency plan;
- enhancing substantially internet capability, including security and capacity management;
- finalising the IT market testing project; and
- developing a five-year capital expenditure plan.

Infrastructure

Planned initiatives to be progressed in 2003-04 include:

- developing strategic planning processes that are linked to Defence's strategic planning, and are fully integrated into other parts of the Group;
- improving the capital facilities planning and contracting processes to allow a 'whole-of-life' approach to planning and managing the estate; and

- incorporating better risk and environmental assessment and management techniques into all business processes, and driving the environmental stewardship agenda across all Defence activities.

Products and Services

One of the key features of the Defence business model is the delivery of an agreed level of performance for a price, with appropriate accountabilities and performance measurement. In line with the implementation of the model, customer service agreements have been established with the majority of internal customers. These agreements outline performance standards for the products and services provided by the Corporate Services and Infrastructure Group.

Industry Engagement

A large proportion of the products and services that Corporate Services and Infrastructure Group provides are delivered by industry. Almost \$2b of products and services are estimated to be delivered under contract in 2003-04. These contracts include the delivery of products and services in the areas shown below:

Table 4.2: Estimated Expenditure on Products and Services' Contracts

Service	Value \$m
Infrastructure investment	359
Information technology and telecommunication services and products	352
Garrison support	335
Housing services	311
Facilities operations	233
Travel services	166
Property services	129
Utilities	95
Training range upgrades	17
Total	1,997

DEFENCE INFORMATION ENVIRONMENT

Further improvements to the efficiency, effectiveness and security of the Defence information environment will be delivered during 2003-04. The goals will be to improve strategic direction and ensure better coordination arrangements for the development, operation and management of Defence information capabilities, especially in developing a network-centric warfare capability.

More effective governance arrangements are enabling the measurement of progress toward these goals, as outlined in the *Defence Information Environment Strategic Plan*, issued for the first time in 2003. The plan also describes strategies for better management of information management risks.

Priorities for 2003-04

Priorities for the period include:

- enhancing the Defence information environment's contributions to Defence capabilities, including command and control and intelligence support capabilities and improving interoperability with our allies and partners;
- developing better funding methodologies for joint information capabilities (both current and future) to ensure they can be balanced and prioritised;
- optimising the acquisition and through-life management of information capabilities;
- embracing a national approach to information management;
- increasing the competence and sustainability of the Defence information environment workforce; and
- improving information assurance by addressing the availability, confidentiality, integrity and accuracy of data.

COMMERCIAL SUPPORT PROGRAM

The Commercial Support Program is a competitive market-testing process which was specifically developed by Defence to suit its capability requirements. The program is a competitive tendering and contracting initiative through which commercial, and sometimes in-house, bids compete for the provision of services. The resulting decisions are determined by what provides the best value for money for Defence. This is a long-term program that will continue to identify activities for market testing as part of a continuous improvement initiative.

The Commercial Support Program encourages efficiency gains across the full spectrum of support activities. This enables the redirection of resources from operationally non-critical areas to combat capability and higher priority activities, thus making a significant contribution to ADF preparedness. Efficiency gains may be delivered not only through contracting out of activities but also through restructuring of in-house arrangements. The most cost-effective means of performing support activities will be determined through competition.

The Commercial Support Program has been used to market test the work of about 16,000 positions since 1991, outsourcing service delivery to industry for 81 of 120 market tests, with about 80 per cent of the tested positions being removed from Defence. The efficiency improvements average approximately 30 per cent of the original costs prior to market testing.

During 2003-04, the result of contract negotiations is expected for ADF health services in Victoria, which follows the decision in October 2002 to outsource this activity. The result of negotiations for the Defence Integrated Distribution System is also expected.

Some 17 identified Commercial Support Program activities will be progressed during 2003-04. These activities, in most cases, are still in the early planning stages.

Table 4.3: Identified Commercial Support Program Activities for 2003-04

ACTIVITY	STATUS
Defence Integrated Distribution System	Contract negotiations continuing.
ADF health services in Victoria	Contract negotiations continuing.
ADF health services in the ACT and southern New South Wales	Bids were not accepted and alternative options are being considered.
ADF health services in Sydney New South Wales region	A draft activity rationalisation review report is being prepared.
ADF health services in Queensland	An activity and rationalisation review is to be carried out.
ADF health services in Northern Territory	An activity and rationalisation review is to be carried out.
ADF health services in West Australia	An activity and rationalisation review is being carried out.
ADF health services in South Australia	An activity and rationalisation review is to be carried out.
ADF health services in Tasmania	An activity and rationalisation review is to be carried out.
ADF rotary wing flying training	The project scope is under assessment.
Amphibious Afloat Ships – fully-contracted integrated materiel support	A draft statement of requirement has been released for comment.
Anzac Ships – fully-contracted integrated materiel support	The project scope is being assessed.
Defence information technology infrastructure services - Central Office – Deakin, Australian Capital Territory	A draft statement of requirement is being developed.
FFG Ships - fully-contracted integrated materiel support	A draft statement of requirement is being developed.
Navy technical training services	The project scope is under assessment and a business case is being finalised.
Personnel services (Corporate Services and Infrastructure Group)	The functions are being rationalised/restructured.
Routine pathology services	The project scope is to be assessed.

PORTFOLIO EVALUATIONS

Portfolio evaluations endorsed by the Defence Audit Committee, in order of priority, for the calendar year 2003 are:

- Review of Defence Leave Policy and Administration;
- Corporate Governance of the Defence Information Environment (Phase 2);
and
- Adventurous Training in the ADF.

A number of evaluations forecast for 2003 will not now proceed:

- The topic, *Implementation of the Balanced Scorecard*, was not endorsed by the Secretary of Defence because, among other matters, a related review is being undertaken within Defence by the Chief Finance Officer.
- The forecast evaluation, *Implementation of the Customer-Supplier Model*, has been deferred until 2004 because of slippages in the full implementation of the model.
- The topic, *Implementation of ADF Personnel Initiatives (the Nunn Review)*, will be reconsidered for inclusion in the 2004-05 portfolio evaluation schedule after a decision on implementing the initiatives recommended in the Nunn Review is made.

Portfolio evaluations agreed in principle by the Defence Audit Committee, in order of priority, for the calendar year 2004 are:

- Effectiveness of the Defence Strategic Workforce Planning Outcomes;
- Implementation of the Customer-Supplier Model; and
- Effectiveness of the Risk Management Framework.

Results from portfolio evaluations conducted in 2002-03 will be reported in the Defence annual report.

